UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE:	*	
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QUIRINO DIPAOLO, JR.,	*	
	*	**CASE NUMBER 02-43161**
	*	
Debtor.	*	
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	*	
STEVEN G. HITZ, *et al*.,	*	
	*	
Plaintiffs,	*	
	*	
vs.	*	**ADVERSARY NUMBER 03-4008**
	*	
QUIRINO DIPAOLO, JR.,	*	
	*	
Defendant.	*	
	*	

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M E M O R A N D U M O P I N I O N
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This cause is before the Court on the complaint of Plaintiffs Steven G. and Valerie C. Hitz ("Plaintiffs") to determine whether a debt is excepted from discharge pursuant to 11 U.S.C. § 523. After being granted leave to file an answer, Debtor/ Defendant Quirino DiPaolo, Jr. ("Defendant") filed his answer. A trial was held on this matter December 15, 2003. Frederick S. Coombs, III, Esq. appeared on behalf of Plaintiffs. Jeffrey D. Adler, Esq. appeared on behalf of Defendant. This Court has juris-diction over this matter pursuant to 28 U.S.C. § 1334(b). This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I). The following constitutes the Court's findings of fact and conclusions of law pursuant to FED. R. BANKR. P. 7052.

F A C T S

On July 3, 2001, Plaintiffs entered into a purchase agree-ment with Builders Incorporated, a general contractor and developer, under which Builders Incorporated would construct a home (herein-after "Home") to be sold to Plaintiffs for the sum of Three Hundred Seventy-Seven Thousand Eight Hundred Fifty Dollars ($377,850.00). (Compl., Ex. A, Purchase Agreement, § 1.) Defendant is the sole shareholder and president of Builders Incorporated. The purchase agreement provided that Builders Incorporated would deliver a general warranty deed and furnish a marketable title to be evidenced by a title guaranty. Defendant and Plaintiff Steven G. Hitz signed the purchase agreement.

The financing agency that Plaintiffs intended to use to fund the purchase, GMAC Mortgage Corporation ("GMAC"), advised Plaintiffs that the previously agreed to mortgage rate could not be guaranteed unless the purchase was closed in February 2002. Accordingly, the parties scheduled the closing for mid-February 2002. However, the Home's construction was not complete. Plain-tiffs and Defendant agreed to close on the Home prior to completion of construction, although an uncommon business practice for Builders Incorporated.

To insure completion of construction and payment of materials, Plaintiffs and GMAC requested Builders Incorporated to deposit Sixty Thousand Dollars ($60,000.00) in escrow from the net proceeds of the sale until Builders Incorporated completed

con-struction of the Home. Upon resistence by Builders Incorporated, the parties agreed that Twenty Thousand Dollars ($20,000.00) of the purchase price would be deposited into an escrow account pending the Home's completion.

On February 12, 2002, Defendant executed an affidavit ("Affidavit") stating that his company, Builders Incorporated, "HA[D] PAID IN FULL FOR ALL WORK PERFORMED AND FOR ALL LABOR, MATERIALS, MACHINERY OR FUEL FURNISHED BY AFFIANT AND ALL SUBCONTRACTORS, MATERIALMEN, AND LABORERS PRIOR TO THE CLOSING DATE, EXCEPT: Fagens/Morgan Dieter." (Compl., Ex. B, Aff., ¶ 1.) Defendant testified that, ordinarily, Builders Incorporated would not make interim payments for labor and supplies mid-construction, but would pay for labor and supplies upon the completion of construction, unless otherwise agreed to with individual service providers. Although aware that construction of the Home was incomplete, Defendant failed to inquire into whether all work and materials had been paid in full prior to closing and prior to signing the Affidavit. In addition, the Affidavit included language that stated Defendant, the affiant, understood that the written Affidavit would be relied on by the title insurance company. Plaintiffs read the Affidavit subsequent to the closing.

In mid-February 2002, the sale closed, Plaintiffs paid in full and received a survivorship deed to the Home with full statutory warranty covenants. As time wore on, Builders Incor-

porated never completed construction of the Home. Accordingly, the Twenty Thousand Dollars ($20,000.00) held in escrow only partially funded the completion of the Home. In addition, beginning in spring 2002, various subcontractors and materialmen filed affidavits asserting unpaid balances and mechanic's liens on Plain-tiffs' Home. Currently, mechanic's liens totaling Forty-Six Thousand Nine Hundred Eight Dollars and 56/100 ($46,908.56) are attributable to work done or materials furnished prior to the execution of Defendant's February 12, 2002 Affidavit.

On May 6, 2002, Plaintiffs filed a complaint in the Court of Common Pleas for Trumbull County, Ohio, Case Number 02-42169, against Builders Incorporated, Defendant, GMAC and Leonard Drenski, Jr., the Home's project manager, for injunctive relief and monetary damages arising from Builders Incorporated's failure to complete construction of the Home and failure to pay the subcontractors. On May 21, 2002, Builders Incorporated filed a Chapter 11 proceeding, staying the Court of Common Pleas action, the date set for the preliminary injunction trial. Defendant filed his own Chapter 7 proceeding on July 19, 2002.

A N A L Y S I S

Section 523(a)(2)(B) provides that a discharge under § 727 of the Bankruptcy Code does not discharge an individual debtor from any debt obtained by the:

> (B) use of a statement in writing–-
>
> (i) that is materially false;
>
> (ii) respecting the debtor's or an insider's financial condition;
>
> (iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
>
> (iv) that the debtor caused to be made or published with intent to deceive[.]

11 U.S.C. § 523(a)(2)(B). A movant must prove each element of § 523(a)(2)(B) by a preponderance of the evidence. *Grogan v. Gar-ner*, 498 U.S. 279, 291 (1991). Thus, pursuant to § 523(a)(2)(B), Plaintiffs must prove that the debt in question was obtained by the use of (1) a written statement; (2) that is materially false; (3) respecting the debtor's or an insider's financial condition; (4) upon which Plaintiffs reasonably relied; (5) that Defendant caused to be published and (6) with the intent to deceive.

First, for a debt to fall within the exception to discharge established by § 523(a)(2)(B), the statement relied upon must be "in writing." In the case at bar, the February 12, 2002 Affidavit prepared by Defendant that attested that, prior to closing, Defendant's company had paid in full for all work performed and materials provided by all subcontractors and laborers except one, was a written document.

Second, the written statement must be materially false to fall within the § 523(a)(2)(B) exception to discharge. "A materially false statement is one that 'paints a substantially untruthful picture of a financial condition by misrepresenting information of the type which would normally affect the decision to grant credit.'" *Jordan v. Southeast Nat'l Bank (In re Jordan)*, 927 F.2d 221, 224 (5th Cir. 1991) (citations omitted). Whether or not the general contractor had paid in full for all work completed and materials used prior to closing would affect the decision of any potential buyer to pay in full because it impacts a buyer's ability to obtain an unencumbered, marketable title. The Affidavit stated that all but one subcontractor had been paid although many sub-contractors had not been paid. Accordingly, the written statement is materially false.

Third, § 523(a)(2)(B) requires the written statement to concern the debtor's or an insider's financial condition to merit exception from discharge. The Bankruptcy Code provides that if the debtor is an individual, as in the case at bar, an insider includes, a "corporation of which the debtor is a director, officer, or person in control[.]" 11 U.S.C. § 101(31)(A)(iv). Builders Incorporated qualifies as an "insider" of Defendant, because Defendant was the president and sole shareholder of Builders Incorporated. The Affidavit asserted that Builders Incorporated had paid all out-standing claims except one, as they

existed as of February 12, 2002, on the Home it was constructing. Thus, the Affidavit concerned an insider's financial condition.

Forth, the creditor must have reasonably relied on the written statement to fall within § 523(a)(2)(B). However, reliance on the written statement can be indirect in certain circumstances. Courts have held that plaintiffs who relied on a credit rating based on a written statement indirectly relied on that written state-ment. *Bell v. Stafos (In re Stafos)*, 666 F.2d 1343 (10th Cir. 1981)*; Rogers v. Gardner*, 226 F.2d 864 (9th Cir. 1955)*; Gen. Elec. Capital Corp. v. Bui (In re Bui)*, 188 B.R. 274 (Bankr. N.D. CA 1995)*; Loyd v. Coyne (In re Coyne)*, 70 B.R. 560 (Bankr. E.D. MO 1987). Those "credit reporting services essentially 're-publish' the false financial statement, and . . . the debtor should be aware that others will rely upon this republication in making credit decisions." *Bui*, 188 B.R. at 280. Similarly, by receiving a marketable title evidenced by a title guarantee, which was made possible because of the Affidavit, Plaintiffs indirectly relied on Defendant's Affidavit that stated all but one outstanding claim had been paid in full. The Affidavit itself recognizes that the written Affidavit would be relied on by title insurance companies. Although Plaintiffs read Defendant's Affidavit subsequent to closing, they nevertheless reasonably relied on the written state-ment at closing when they (i) paid the full purchase price for a

marketable title, evidenced by the title insurance company, and (ii) agreed to put only Twenty Thousand Dollars ($20,000.00) into escrow to cover the completion of the Home's construction.

Fifth, a debtor must have caused the written statement to be published to fall within § 523(a)(2)(B). Defendant published the Affidavit when the Affidavit was used to provide marketable title.

Sixth, a debtor's false statement in writing must be written with an intent to deceive to warrant a finding that the debt is nondischargeable under § 523(a)(2)(B). The Sixth Circuit has held that this requirement is met if a debtor is grossly reckless as to the truth of the written statement. *Investors Credit Corp. v. Batie* (*In re Batie*), 995 F.2d 85 (6th Cir. 1993). Defendant acted with grossly reckless disregard when he failed to inquire into whether any bills for labor or materials were outstanding, although aware that the Home was incomplete and that Builders Incorporated usually paid for labor and materials upon completion of each residence. In addition, Defendant never made any attempt to pay the subcontractors after swearing under oath in the written Affidavit that all but one were paid in full.

Upon review of the record on the whole, the Court finds that Plaintiffs have met their burden of establishing the elements of § 523(a)(2)(B). Accordingly, the debt is nondischargeable. The pending case in the Court of Common Pleas

for Trumbull County, Ohio, is the appropriate forum to determine what, if any, damages Plaintiffs have incurred.

An appropriate order shall enter.

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HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

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QUIRINO DIPAOLO, JR.,	*	
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Defendant.	*	
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O R D E R

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For the reasons set forth in this Court's memorandum opinion entered this date, judgment in favor of Plaintiffs Steven G. and Valerie C. Hitz is entered. Defendant's debt to Plaintiffs is nondischargeable under 11 U.S.C. § 523(a)(2)(B). The pending case in the Court of Common Pleas for Trumbull County, Ohio, is the appropriate forum to determine what, if any, damages Plaintiffs have incurred.

IT IS SO ORDERED.

_____

HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Memorandum Opinion and Order were placed in the United States Mail this _____ day of August, 2004, addressed to:

STEVEN G. and VALERIE C. HITZ, 2295 Keystone Trail, Cortland, OH 44410.

FREDERICK S. COOMBS, III, ESQ., 26 Market Street, Suite 1200, Youngstown, OH 44503.

QUIRINO DIPAOLO, JR., 8551 Hunters Trail, Warren, OH 44484.

JEFFREY D. ADLER, ESQ., 973 W. Liberty Street, Suite C, Hubbard, OH 44425.

MICHAEL D. BUZULENCIA, ESQ., 150 East Market Street, Suite 300, Warren, OH 44481.

DAVID A. SHEPHERD, ESQ., 185 High Street, N.E., Warren, OH 44481.

SAUL EISEN, United States Trustee, BP America Building, 200 Public Square, 20th Floor, Suite 3300, Cleveland, OH 44114.

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JOANNA M. ARMSTRONG